DEPARTMENT OF STATE REVENUE

04-20110417.LOF

Letter of Findings Number: 04-20110417
Sales and Use Tax
For Tax Years 2008 and 2009

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ISSUES

I. Sales and Use Tax–Manufacturing Exemption.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-5-3; IC § 6-2.5-5-9; IC § 6-2.5-5-30; IC § 6-8.1-5-1; Clean Air Act, 42 U.S.C. § 7401, et seq. (2007); 40 CFR § 70.1, et seq. (2007); 45 IAC 2.2-5-6; 45 IAC 2.2-5-8; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Rhoade v. Indiana Dep't of State Revenue, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); Indiana Dep't of State Revenue v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); General Motors Corp. v. Indiana Dep't. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991); Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676 (Ind. Ct. App.1980); Indiana Dep't. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983); Department of Revenue v. U. S. Steel Corp., 425 N.E.2d 659 (Ind. Ct. App. 1981); Graham Creek Farms v. Indiana Dep't of State Revenue, 819 N.E.2d 151 (Ind. Tax Ct. 2004).

Taxpayer protests the assessment of use tax on certain of its purchases.

II. Sales and Use Tax–Environmental Exemption.

Authority: IC § 6-2.5-3-2; IC § 6-2.5-5-30; IC § 6-8.1-5-1; Clean Air Act, 42 U.S.C. § 7401, et seq. (2007); 40 CFR § 70.1, et seq. (2007).

Taxpayer protests the assessment of use tax on its purchases of hydrated lime, sodium chloride, and titanium dioxide.

III. Sales and Use Tax–Services.

Authority: IC § 6-2.5-1-1; IC § 6-2.5-1-2; IC § 6-2.5-3-2; IC § 6-2.5-4-1; IC § 6-8.1-5-1; 45 IAC 2.2-1-1; 45 IAC 2.2-4-1.

Taxpayer protests the assessment of use tax on its purchase of a service.

STATEMENT OF FACTS

Taxpayer is an Indiana manufacturer. After an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer owed use tax for the tax years 2008 and 2009. The Department found that Taxpayer had made a variety of purchases on which the Indiana sales tax was not paid at the time of purchase nor was use tax remitted to the Department. Taxpayer protested the assessment of use tax on certain of its purchases. An administrative hearing was held, and this Letter of Findings results.

I. Sales and Use Tax–Manufacturing Exemption.

DISCUSSION

Taxpayer asserts that certain of its purchases are not subject to use tax because the purchases would qualify for the manufacturing equipment exemption as found in IC § 6-2.5-5-3.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). "Use" means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a). The use tax is functionally equivalent to the sales tax. See Rhoade v. Indiana Dep't of State Revenue, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

Generally, all purchases of tangible personal property by persons engaged in the direct production, manufacture, fabrication, assembly, or finishing of tangible personal property are taxable. 45 IAC 2.2-5-8(a). An exemption from use tax is granted for transactions where the sales tax was paid at the time of purchase pursuant to IC § 6-2.5-3-4. There are also additional exemptions from sales tax and use tax. A statute which provides a tax exemption, however, is strictly construed against the taxpayer. Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "Exemption statutes are strictly construed because an exemption releases property from the obligation of bearing its fair share of the cost of government." General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991) aff'd 599 N.E.2d 588 (Ind. 1992) (Internal citations omitted). Thus, "[W]here such an exemption is claimed, the party claiming the same

must show a case, by sufficient evidence, which is clearly within the exact letter of the law." RCA, 310 N.E.2d at 100-101. Accordingly, the taxpayer claiming exemption has the burden of showing the terms of the exemption statute are met. General Motors, 578 N.E.2d at 404.

IC § 6-2.5-5-3(b) states:

> Transactions involving manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it **for direct use in the direct production, manufacture**, fabrication, assembly, extraction, mining, processing, refining, or finishing **of other tangible personal property**. (**Emphasis added**).

Thus, the legislature granted Indiana manufacturers a sales tax exemption for certain purchases, which are for "direct use in direct production, manufacture... of other tangible personal property." In enacting the exemption, the legislature clearly did not intend to create a global exemption for any and all equipment which a manufacturer purchases for use within its manufacturing facility. "Fairly read, the exemption was meant to apply to capital equipment that meets the 'double direct' test." Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676, 678 (Ind. Ct. App. 1980). The capital equipment "in order to be exempt, must (1) be directly used by the purchaser and (2) be used in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of tangible personal property." Indiana Dep't. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520, 525 (Ind. 1983). The Cave Stone court found that the "focus of analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Id. "The test for directness requires the equipment to have an 'immediate link with the product being 'produced.'" Id. Accordingly, the sales tax exemption is applicable to that equipment which meets the "double direct" test and is "essential and integral" to the manufacture of taxpayer's tangible personal property. General Motors, 578 N.E.2d at 401. The application of Indiana's double-direct manufacturing exemptions often varies based on a determination of when a taxpayer's manufacturing process is considered to have begun and ended.

An exemption applies to manufacturing machinery, tools, and equipment directly used by the purchaser in direct production. 45 IAC 2.2-5-8(a). Machinery, tools, and equipment acquired for "direct use in the direct production" is defined in 45 IAC 2.2-5-8(c) as "manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process" that have "an immediate effect on the article being produced." Property has "an immediate effect" when it becomes "an essential and integral part of the integrated process which produces tangible personal property." 45 IAC 2.2-5-8(c). 45 IAC 2.2-5-8(d) excludes pre-production and post production activities by providing that "'direct use in the production process' begins at the point of first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its complete form."

45 IAC 2.2-5-8(g) further states:

> "Have an immediate effect upon the article being produced": Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has an immediate effect upon the article being produced". Instead, in addition to being essential for one of the above reasons, the property must also be an integral part of an integrated process which produces tangible personal property.

Additionally, 45 IAC 2.2-5-8 (j) provides:

> Machinery, tools, and equipment used in managerial sales, research, and development, or other non-operational activities, are not directly used in manufacturing and, therefore, are subject to tax. This category includes, but is not limited to, tangible personal property used in any of the following activities: management and administration; selling and marketing; exhibition of manufactured or processed products; safety or fire prevention equipment which does not have an immediate effect on the product; space heating; ventilation and cooling for general temperature control; illumination; heating equipment for general temperature control; and shipping and loading.

Accordingly, machinery and equipment for the use in the production of a manufactured good is subject to sales and use tax unless the property used has an immediate effect on and is essential to the production of the marketable good. Thus, it is only the property that has an immediate effect on and is essential to the production that is directly used in the direct production of a marketable good and is exempt.

A. "Chip Dryers and Conveyor System."

The Department found that use tax was due on the purchases of repair and replacement parts for the "chip dryers" and parts used to extend the "conveyor system." The Department determined that Taxpayer's uses of the "chip dryers and conveyor system" were pre-production activities. The audit report states "the chip dryers are used prior to the first step of production, which would begin at the furnaces when the raw materials are poured in and are melted down.

Taxpayer asserts that its purchases of the "chip dryer repair and replacement parts" and the parts used to

extend the "conveyor system" are exempt manufacturing equipment.

1. "Chip Dryers."

Taxpayer maintains that since the "chip dryer" removes the foreign materials from the aluminum, it changes the product and is exempt.

As provided above, the court found that the "focus of analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. While the "chip dryers" may make purification of recycled aluminum more efficient, it is not equipment that has an immediate effect on the manufactured ingot. The "chip dryers" ready a raw material, recycled aluminum, for the manufacturing process. Thus, the "chip dryer" is a separate system both distinct and removed from the actual manufacturing of the aluminum ingot. The "chip dryers" simply function to treat the recycled aluminum before the aluminum enters into the manufacturing process. Accordingly, the processing of the recycled aluminum is a preproduction activity and does not fall under the exemption.

However, Taxpayer's purchases of the "chip dryers" were required by the Indiana Department of Environmental Management ("IDEM"). The "chip dryers" are listed as some of the equipment that IDEM required Taxpayer to purchase before Taxpayer could receive a "Title V Environmental Permit" from the Environmental Protection Agency under Title V of the Clean Air Act. See Clean Air Act, 42 U.S.C. § 7401, et seq. (2007) & 40 CFR § 70.1, et seq. (2007). Since the "environmental control equipment" was required by IDEM, the repair and replacement parts purchased for this equipment are exempt under the "environmental exemption" as defined in IC § 6-2.5-5-30.

IC § 6-2.5-5-30, in relevant part, provides:

Sales of tangible personal property are exempt from the state gross retail tax if:

(1) the property constitutes, is incorporated into, or is consumed in the operation of, a device, facility, or structure predominately used and acquired for the purpose of complying with any state, local, or federal environmental quality statutes, regulations or standards; and

(2) the person acquiring the property is engaged in the business of manufacturing, processing, refining, mining, or agriculture.

(Emphasis added).

While Taxpayer has not provided sufficient documentation to support its assertion that the "chip dryers" qualify for the "manufacturing equipment exemption," Taxpayer has provided sufficient documentation to establish that the "chip dryers" were purchased to comply with an environmental quality standard and are exempt from sales and use tax under the "environmental exemption" as defined in IC § 6-2.5-5-30. Therefore, the purchase of repair and replacement parts for the "chip dryers" would qualify for this exemption as well.

Accordingly, Taxpayer's protest to the imposition of use tax on its purchases of repair and replacement parts for the "chip dryers" is sustained.

2. "Conveyor Systems."

Taxpayer asserts that its "conveyor systems" that feed the recycled aluminum into the "chip dryers" is manufacturing equipment. The "conveyor systems" move the recycled aluminum from storage into the "chip dryers." Taxpayer maintains that since the "conveyor systems" continuously feeds an ingredient of the final product into the "chip dryers," the "conveyor systems" are part of the manufacturing process. Taxpayer reasons that since these items of machinery are part of the manufacturing process, then they are used in direct production and are exempt.

While the "conveyor systems" may be a necessary part of Taxpayer's manufacturing process, the devices are not machinery that has an immediate effect on the manufactured product. The "conveyor systems" simply function to transport a raw material during pre-production. Therefore, the transporting of the recycled aluminum by the "conveyor systems" is a pre-production activity and does not fall under the exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on parts used to extend the "conveyor systems" is respectfully denied.

B. "Testing and Inspection Equipment."

The Department found that use tax was due on the Taxpayer's purchases of a pyrometer, a spectrometer, and a "maintenance agreement" for the spectrometer. Taxpayer asserts that the pyrometer and the spectrometer are exempt manufacturing equipment. Taxpayer maintains that these purchases are testing and inspection machinery and equipment which are essential and integral to Taxpayer's integrated production process. Taxpayer points to 45 IAC 2.2-5-8(i) as support for its argument that the "machinery and equipment" at issue are exempt.

45 IAC 2.2-5-8(i) states:

Testing and inspection. Machinery, tools, and equipment used to test and inspect the product as part of the production process are exempt.

–EXAMPLE–

Selected parts are removed from production according to a schedule dictated by statistical sampling methods. Quality control equipment is used to test the parts in a room in the plant separate from the production line. Because of the functional interrelationship between the testing equipment and the machinery on the production line and because of the product flow, the testing equipment is an integral part of the

integrated production process and is exempt.

Accordingly, not all testing and inspecting equipment would qualify for exemption. The testing and inspecting equipment must have a functional interrelationship with the machinery on the product line and the product flowing in production to qualify for the manufacturing equipment exemption. Thus, testing and inspecting that take place prior to or after production is complete would not qualify.

1. Pyrometer.

Taxpayer maintains that six purchases from "Pyrotek," where the auditor made a notation that the items were for portable pyrometer(s), are exempt manufacturing equipment. Taxpayer also noted that a purchase by another vendor in the amount of $6,750 (paid with check number 65572) where the auditor made a notation that "no description of item purchased [was provided]" as related to the pyrometer. However, Taxpayer first referred to this purchase as relating to another matter and, therefore, this $6,750 purchase is addressed in Issue III. This discussion will only address the six "Pyrotek" purchases. Taxpayer states, "The pyrometer is used to determine the temperature of the aluminum ingots being produced. Proper temperature verification is needed to ensure proper melting and mixture of the various raw materials."

While Taxpayer did not provide any documentation supporting its assertion regarding the use of its purchases, the Department in the course of its research happened to find that a pyrometer is the instrument used to measure the temperature of molten aluminum. Therefore, the pyrometer would be equipment directly used during the production process and qualifies for the manufacturing equipment exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on its six "Pyrotek" purchases for portable pyrometers is sustained.

2. Spectrometer and Spectrometer "Maintenance Agreement."

Taxpayer maintains that the spectrometer is exempt manufacturing equipment. Taxpayer states, "The spectrometer uses light rays to check and verify the chemical composition [of] the aluminum ingots." Additionally, Taxpayer maintains that the payments made for the service contract covering the coolant spectrometer qualify for exemption under 45 IAC 2.2-5-8. In effect, Taxpayer asserts that the property furnished under the "maintenance agreement" would be considered a repair or replacement part for the spectrometer.

Pursuant to 45 IAC 2.2-5-8(h)(2), "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the equipment would be tax exempt to the extent that the equipment is exempt.

However, Taxpayer has not provided any information/documentation beyond its assertion that the spectrometer is used somewhere in its production process. Without specific information about where and how the equipment is used during the production process, a determination about the exempt status of the equipment cannot be made. Therefore, Taxpayer has not provided sufficient information to demonstrate that the spectrometer is directly used in Taxpayer's production of its goods or that it has "an immediate effect on the article being produced."

Accordingly, Taxpayer's protest to the imposition of use tax on the spectrometer and the spectrometer maintenance agreement is respectfully denied.

C. "Safety Clothing and Equipment."

The Department determined that use tax was due on Taxpayer's rental of uniforms and safety glasses. The Department conducted an onsite investigation of Taxpayer's facility, and concluded that the uniforms Taxpayer purchased were for the comfort or convenience of the personnel. The audit report, on pages 5-6, states:

> Per the taxpayer, all hourly employees are required to wear their uniforms at all times while working on their jobs whether it be non-production or production area of the facility. Additionally, salaried employees must wear them if working in the plant, but can also wear them full-time if they choose. Full uniforms are issued to all hourly employees, plus the Production General Manager and Manager, the Shipping & Receiving Manager, and the Maintenance Manager. Partial uniforms are issued to the Shipping & Receiving, Sales[] and Purchasing General Managers, the Compliance General Manager, and the QA Technician for use as needed. Temporary workers are issued full uniforms depending upon how long they have worked at the company.
>
> ...
>
> The uniforms are the typical knit-type work shirts and pants used within the manufacturing industry but are constructed of fibers and fabrics specifically designed to withstand extreme temperatures, will resist ignition, self-extinguish and not melt.
>
> During the tour of the facilities on two separate occasions, no uniforms were required to be worn before proceeding with the tour of the facilities. Additionally no face protection other than safety glasses and a hard hat were required in the facility. The tour gave an up close look at the facility and the overall process there and went through both production and non-production areas. The tour did allow for close proximity to high-temperature areas such as furnaces, the troughs for the hot, molten aluminum, and the areas where the casting was done....
>
> ...

Sales tax was not collected on the rental of [the uniforms]. Additionally, the taxpayer did not self-assess and remit use tax on the rental of the tangible personal property. Because the uniform were worn by everyone in the facility, no uniform was required for either the plant tours, and because no tax was paid at the time the uniforms were rented, use tax is due upon the rental of such property.

Taxpayer maintains that the uniforms and safety glasses are "safety clothing and equipment" and qualify for an exemption from use tax.

45 IAC 2.2-5-8(c) states in relevant part that:

The state gross retail tax does not apply to purchases of manufacturing machinery, tools, and equipment to be **directly used by the purchaser in the production process provided that such machinery, tools, and equipment are directly used in the production process**; i.e., they have an immediate effect on the article being produced. Property has an immediate effect on the article being produced if it is an essential and integral part of an integrated process which produces tangible personal property.

–EXAMPLES–

...

(2) **The following types of equipment constitute essential and integral parts of the integrated production process and are, therefore, exempt. The fact that such equipment may not touch the work-in-process or, by itself, cause a change in the product, is not determinative**.

...

(F) **Safety clothing or equipment which is required to allow a worker to participate in the production process without injury or to prevent contamination of the product during production**.

(**Emphasis added**).

In Department of Revenue v. U. S. Steel Corp., 425 N.E.2d 659 (Ind. Ct. App. 1981), the appellate court affirmed the trial court's findings, in favor of the taxpayer, U.S. Steel Corp., that it was entitled to the manufacturing exemption for its purchases of personal protective equipment, including, but not limited to, prescription safety eyeglasses, protective mittens, hardhats, goggles, masks, hoods, jackets and aprons. The U.S. Steel court refined the application of the "double direct standard" illustrated in Indiana Dep't of State Revenue v. Harrison Steel Casting, 402 N.E.2d 1276 (Ind. Ct. App. 1980) and focused on "whether the safety equipment is an integral part of manufacturing and operates directly on the product during production."

Acknowledging that the "U.S. Steel's safety equipment was one of the tools used by workers to accomplish the job," The U.S. Steel court concluded that:

Since steel can be made only because shielded workers deal directly with the raw materials of the product, the shields not only protect the worker but are a part of manufacturing which operates directly on the product during production.

U.S. Steel, 425 N.E.2d at 664.

As 45 IAC 2.2-5-8(g) explains, however, "The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property has an immediate effect upon the article being produced." (Internal quotation marks omitted).

In U.S. Steel, but for the shields, the workers would not have been able to directly handle the materials used in the production process. While Taxpayer states it requires its workers to wear the safety glasses and uniforms, Taxpayer, however, has not established how the safety glasses and uniforms relate to allowing the workers to participate in the production process without injury. The Department conducted an onsite investigation during the audit. The Department concluded that the uniforms and safety glasses Taxpayer purchased were for the comfort or convenience of the personnel. Even if that description were not accurate, Taxpayer has not adequately established how these items are "required" for the workers to safely participate in the production process. While the safety glasses and uniforms existence might provide the assurance of a safer operating environment, nonetheless, Taxpayer has not provided enough information to demonstrate that the safety glasses and uniforms are identical to the shields in U.S. Steel discussed above. Therefore, Taxpayer has not met its burden to show that the safety glasses and uniforms were used in a manner that qualifies for the exemption from sales tax.

Accordingly, Taxpayer's protest to the imposition of use tax on the safety glasses and uniform rentals is respectfully denied.

D. "Transportation Equipment."

The Department found that use tax was due on seventy-seven percent of Taxpayer's forklift purchases. Taxpayer asserts that its forklift purchases qualify for a forty percent exemption from use tax. Taxpayer maintains that a prior audit determined this percentage and the current audit should not be able to change this determination.

Under 45 IAC 2.2-5-8(f)(2), which states that "[t]ransportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process."

The Department conducted an onsite investigation during the audit and gave detailed information about the number of forklifts and how each of the forklifts was used by Taxpayer. The Department concluded that the forklift

purchases qualified for a twenty-three percent exemption. Taxpayer has not provided enough information to demonstration that the forklifts qualify for an additional exemption amount. The prior audit was conducted in 1999 and covered Taxpayer operations during 1996 to 1998.

However, Taxpayer has not provided any information/documentation beyond its general assertion that the forklift purchases qualify for a forty percent exemption similar to the purchases made in the prior audit. Taxpayer failed to develop this argument and failed to provide specific information about the prior audit compared to the current audit. For example, Taxpayer did not address whether the number of forklifts was the same, whether the activities performed by forklifts were the same, or whether the activities performed by the forklifts were performed for the same amount of time. Additionally, Taxpayer did not suggest any errors were made by the Department in its analysis of the forklift activities in arriving at the seventy-seven percent taxable amount. Therefore, Taxpayer has not provided sufficient information to demonstrate that the "forklift purchases" qualify for more than the twenty-three percent exemption given during the audit.

Accordingly, Taxpayer's protest to the imposition of use tax on seventy-seven percent of its forklift purchases is respectfully denied.

E. "Furnace Platform and Steel Wall."

The Department found that use tax was due on Taxpayer's purchases of a "furnace platform" and a "steel wall." Taxpayer maintains that the "furnace platform" and "steel wall" are "directly related to the furnace itself" and qualify for the manufacturing equipment exemption.

Taxpayer failed to develop this argument and failed to specifically address this argument during the hearing. Without specific information about where and how the "furnace platform" and a "steel wall" are used during the production process, a determination about the exempt status of the "furnace platform" and "steel wall" cannot be made. Therefore, Taxpayer has not provided sufficient information to demonstrate that the "furnace platform" and a "steel wall" are directly used in Taxpayer's production of its goods or that it has "an immediate effect on the article being produced."

Accordingly, Taxpayer's protest to the imposition of use tax on the "furnace platform" and the "steel wall" is respectfully denied.

F. "PP2 and EF-4."

Initially, Taxpayer's protest letter stated that the "PP2 and EF-4" are "directly related to the melting furnaces" and should be exempt. Subsequently, Taxpayer submitted a letter that stated that the "PP2" controls the chip dryer. After the hearing, Taxpayer presented a picture which showed four electric control panels labeled PP2 one of which was labeled roof exhaust fan, a clock, and a fire blanket.

As Example 5 of 45 IAC 2.2-5-8(g) illustrates, power supply equipment may be used for exempt and non-exempt purposes in the manufacturing process. Specifically Example 5 of 45 IAC 2.2-5-8(g) states, "Switch gears, transformers, conduits, cables, controls, rectifiers, and generators which are interconnect with the production equipment and serve as an electrical distribution system for such equipment are exempt from tax. Items used to distribute electricity for general lighting and space heating are taxable."

Taxpayer failed to develop this argument and failed to specifically address this argument during the hearing. Without specific information about where and how the "PP2 and EF-4" are used during the production process, a determination about the exempt status of the "PP2 and EF-4" cannot be made. Therefore, Taxpayer has not provided sufficient information to demonstrate that the "PP2 and EF-4" are directly used in Taxpayer's production of its goods or that it has "an immediate effect on the article being produced."

Accordingly, Taxpayer's protest to the imposition of use tax on the "PP2 and EF-4" is respectfully denied.

G. "Slag Boxes."

The Department found that use tax was due on Taxpayer's purchase of "slag boxes." Taxpayer maintains that the "slag boxes" are used to accumulate and store molten waste and allow it to cool and, therefore, qualify for the manufacturing equipment exemption.

While equipment that is used to actually extract the waste from the production process can qualify for the manufacturing exemption, any equipment that is used to collect, transport, store, or otherwise process the waste after its extraction is subject to tax. See Graham Creek Farms v. Indiana Dep't of State Revenue, 819 N.E.2d 151 (Ind. Tax Ct. 2004) (exempting equipment that actually remove waste from the production process, but not extending the exemption to equipment that is used to transport the waste that has been removed from production.) Since the "slag boxes" are used to collect, store, and transport waste of the manufacturing process that has been extracted from the production process, the "slag boxes" are used in a post-production activity and are taxable.

Accordingly, Taxpayer's protest to the imposition of use tax on the "slag boxes" is respectfully denied.

H. "Cribbing."

The Department found that use tax was due on Taxpayer's purchase of "cribbing." Taxpayer maintains that the "cribbing" is metal banding used to secure the aluminum ingots that are produced by Taxpayer and qualify for the nonreturnable containers exemption.

IC § 6-2.5-5-9(d) provides:

Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person

acquiring the material or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

In addition, 45 IAC 2.2-5-16, in its relevant parts, states:

(a) The state gross retail tax shall not apply to sales of nonreturnable wrapping materials and empty containers to be used by the purchaser as enclosures or containers for selling contents to be added, and returnable containers containing contents sold in a sale constituting selling at retail and returnable containers sold empty for refilling.

(b) In general the gross proceeds from the sale of tangible personal property in a transaction of a retail merchant constituting selling at retail are taxable. This regulation [45 IAC 2.2] provided an exemption for wrapping materials and containers.

(c) General rule. The receipt from a sale by a retail merchant of the following types of tangible personal property are exempt from state gross retail tax:

(1) Nonreturnable containers and wrapping materials including steel strap and shipping pallets to be used by the purchaser as enclosures for selling tangible personal property.

...

(d) Application of general rule.

(1) Nonreturnable wrapping material and empty containers. To qualify for this exemption, nonreturnable wrapping materials and empty containers must be used by the purchaser in the following way:

(A) The purchaser must add contents to the containers purchased; and

(B) The purchaser must sell the contents added.

...

Thus, the nonreturnable container and packing exemption is provided for wrapping materials or containers that act to enclose or contain a product. During the protest, Taxpayer presented documentation, including pictures, demonstrating Taxpayer's use of the "cribbing." "Cribbing" consists of metal straps that hold the stacks of aluminum ingots on the pallets. The "cribbing" in question in this protest is analogous to the steel straps discussed in 45 IAC 2.2-5-16(c)(1) that acts to enclose or contain a product. Therefore, the "cribbing" at issue qualifies for the nonreturnable container exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on the "cribbing" is sustained.

I. "Digital Indicators and Accessories."

The Department found that use tax was due on Taxpayer's purchase of "digital indicators and accessories," including the "digital weight indicators," a "loadcell foot," a printer, a printer cable, a printer program, carbonless printable scale tickets, and printer ribbons. Taxpayer states that "the items related to the digital indicator, digital weight indicators, and the related accessories are used during the melting and subsequent placement of molten aluminum into their cooling containers to ensure each bar is of the proper weight, and to keep track of the total weight for any particular stack during the production process." Taxpayer maintains that these items would qualify for the manufacturing equipment exemption.

Taxpayer has not provided any information/documentation beyond its general assertion that the "digital indicators and accessories" are used somewhere during "melting" and other production processes. Taxpayer failed to develop this argument and failed to specifically address this argument during the hearing. Without specific information about where and how the equipment is used during the production process, a determination about the exempt status of the equipment cannot be made. Therefore, Taxpayer has not provided sufficient information to demonstrate that the "digital indicators and accessories" are directly used in Taxpayer's production of its goods or that it has "an immediate effect on the article being produced."

Accordingly, Taxpayer's protest to the imposition of use tax on "digital indicators and accessories" is respectfully denied.

J. "Paperless Recorder," "DC Input Module," and "CF Card."

The Department found that use tax was due on Taxpayer's purchase of a "paperless recorder," a "DC input module," and a "CF card." Taxpayer states that "these items are physically attached to the 'M' and 'H' furnaces and are used to track the performance of the respective furnace combustion systems to ensure proper performance." Taxpayer maintains that these items would qualify for the manufacturing equipment exemption.

Taxpayer has not provided any information/documentation beyond its general assertion that the "paperless recorder," a "DC input module," and a "CF card" are used in connection with its furnaces. Taxpayer failed to develop this argument and failed to specifically address this argument during the hearing. Without specific information about where and how the equipment is used during the production process, a determination about the exempt status of the equipment cannot be made. Additionally, the description provided by Taxpayer appears to refer to equipment that would be used for maintenance of the furnaces, which is a taxable, non-production activity. Therefore, Taxpayer has not provided sufficient information to demonstrate that the "paperless recorder," a "DC input module," and a "CF card" are directly used in Taxpayer's production of its goods or that it has "an immediate effect on the article being produced."

Accordingly, Taxpayer's protest to the imposition of use tax on the "paperless recorder," a "DC input module," and a "CF card" is respectfully denied.

FINDING

Taxpayer's protest to the imposition of use tax on "manufacturing equipment" is sustained in part and denied in part. Taxpayer's protest to the imposition of use tax on repair and replacement parts for the "chip dryers" is sustained, as discussed in subpart A(1). Taxpayer's protest to the imposition of use tax on parts used to extend the "conveyor systems" is respectfully denied, as discussed in subpart A(2). Taxpayer's protest to the imposition of use tax on its six "Pyrotek" purchases for portable pyrometers is sustained, as discussed in subpart B(1). Taxpayer's protest to the imposition of use tax on the spectrometer and the spectrometer maintenance agreement is respectfully denied, as discussed in subpart B(2). Accordingly, Taxpayer's protest to the imposition of use tax on the safety glasses and uniform rentals is respectfully denied, as discussed in subpart C. Taxpayer's protest to the imposition of use tax on seventy-seven percent of its forklift purchases is respectfully denied, as discussed in subpart D. Taxpayer's protest to the imposition of use tax on the "furnace platform" and a "steel wall" is respectfully denied, as discussed in subpart E. Taxpayer's protest to the imposition of use tax on the "PP2 and EF-4" is respectfully denied, as discussed in subpart F. Taxpayer's protest to the imposition of use tax on the "slag boxes" is respectfully denied, as discussed in subpart G. Taxpayer's protest to the imposition of use tax on "cribbing" is sustained, as discussed in subpart H. Taxpayer's protest to the imposition of use tax on "digital indicators and accessories" is respectfully denied, as discussed in subpart I. Taxpayer's protest to the imposition of use tax on the "paperless recorder," a "DC input module," and a "CF card" is respectfully denied, as discussed in subpart J.

II. Sales and Use Tax–Environmental Exemption.

DISCUSSION

The Department found that use tax was due on the purchases of hydrated lime, sodium chloride, and titanium dioxide that Taxpayer had made without paying sales tax. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Again, the Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

Taxpayer maintains that the hydrated lime, sodium chloride, and titanium dioxide were purchased for disposing of its "molten waste." Taxpayer asserts that the Indiana Department of Environmental Management ("IDEM") required Taxpayer to install "environment control equipment" in which the lime is used to coat the "molten waste" and the sodium chloride and titanium oxide are used to coat the containers that hold the "molten waste." Taxpayer asserts that the Indiana Department of Environmental Management ("IDEM") required Taxpayer to install the "environmental control equipment" before Taxpayer could receive a "Title V Environmental Permit" from the Environmental Protection Agency under Title V of the Clean Air Act. See Clean Air Act, 42 U.S.C. § 7401, et seq. (2007) & 40 CFR § 70.1, et seq. (2007). Taxpayer reasons that since the "environmental control equipment" was required by the IDEM then the chemicals purchased for use in conjunction with this equipment are exempt under the "environmental exemption" as defined in IC § 6-2.5-5-30.

IC § 6-2.5-5-30, in relevant part, provides:

Sales of tangible personal property are exempt from the state gross retail tax if:

(1) the property constitutes, is incorporated into, or is consumed in the operation of, a device, facility, or structure predominately used and acquired for the purpose of complying with any state, local, or federal environmental quality statutes, regulations or standards; and

(2) the person acquiring the property is engaged in the business of manufacturing, processing, refining, mining, or agriculture. (Emphasis added).

During the hearing, the Taxpayer presented the permit report issued by IDEM. The hydrated lime was specifically listed as necessary for use with two "reverberatory furnaces" that IDEM required Taxpayer to purchase. Therefore, Taxpayer has provided sufficient documentation to support its assertion that the hydrated lime was purchased to comply with an environmental quality standard and are exempt from sales and use tax under the "environmental exemption" as defined in IC § 6-2.5-5-30. However, neither the sodium chloride nor the titanium dioxide were as required by IDEM. Therefore, Taxpayer has failed to provide sufficient documentation to support its assertion that the sodium chloride and the titanium dioxide were purchased to comply with an environmental quality standard.

FINDING

Taxpayer's protest to the imposition of use tax on its purchases of hydrated lime is sustained. However, Taxpayer's protest to the imposition of use tax on its purchases of sodium chloride and titanium dioxide is respectfully denied.

III. Sales/Use Tax–Services.

DISCUSSION

The Department found that use tax was due on Taxpayer's $6,750 purchase (paid with check number 65572) where the auditor made a notation that "no description of item purchased [was provided]." At the time of the audit, the auditor was unable to verify the nature of the transaction and whether Taxpayer paid sales tax at the time of the sales transaction, and, therefore, assessed use tax on the purchase. As stated previously, Indiana imposes

"an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Again, the Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

Taxpayer asserts that the Department's assessment of use tax on this $6,750 purchase where the auditor made a notation that "no description of item purchased [was provided]" is incorrect because it is a transaction exempt from use tax. Taxpayer maintains that this amount represents a charge for a service, and, therefore, is not subject to use tax. During the hearing, Taxpayer referred to an email from an employee of Taxpayer to the auditor that said the invoiced amount was for the "dryout of the 'H' Furnace floor as part of normal repairs and maintenance." Taxpayer did not provide the email from the employee. However, even if Taxpayer had provided the email from the employee, Taxpayer failed to provide documentation to support the assertions of the employee. While an email from an employee can be a helpful tool to explain other documentation, an email alone is self-serving and is insufficient to rebut the presumption of the Department's assessment.

Nonetheless, even taking Taxpayer's assertions at face value, the mere fact that a transaction might have a service component is not determinative. Pursuant to IC § 6-2.5-4-1(e), the amount of the retail transaction that is subject to sales tax includes "the price of the property transferred" and "any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records." Further, 45 IAC 2.2-4-1(b)(3) provides that the amount of the retail transaction that is subject to tax includes the amounts collected for "services performed or work done on behalf of the seller prior to transfer of such property at retail." Thus, when services are performed or work is done to tangible personal property before the tangible personal property is transferred to the purchaser, the amount of the charges for the services or work done is also subject to sales tax.

Moreover, services that are performed as part of a retail "unitary transaction" are subject to sales and use tax. IC § 6-2.5-1-2(b). A retail "unitary transaction" is one in which items of personal property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC § 6-2.5-1-1(a). A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. 45 IAC 2.2-1-1(a). Therefore, Taxpayer has failed to meet its burden under IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest to the imposition of use tax on "services" is respectfully denied.

SUMMARY

Taxpayer's protest to the imposition of use tax on repair and replacement parts for the "chip dryers" is sustained, as discussed in Issue A(1). Taxpayer's protest to the imposition of use tax on its six "Pyrotek" purchases for portable pyrometers is sustained, as discussed in Issue B(1). Taxpayer's protest to the imposition of use tax on "cribbing" is sustained, as discussed in Issue I(H). Taxpayer's protest to the imposition of use tax on its purchases of hydrated lime is sustained, as discussed in Issue II. In all other respects, Taxpayer's protest is denied.

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